

§ 1.174-3

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any deposit of ore, oil, gas or other mineral. See sections 617 and 263.

[T.D. 6500, 25 FR 11402, Nov. 26, 1960, as amended by T.D. 8562, 59 FR 50160, Oct. 3, 1994]

§ 1.174-3 Treatment as expenses.

(a) *In general.* Research or experimental expenditures paid or incurred by a taxpayer during the taxable year in connection with his trade or business are deductible as expenses, and are not chargeable to capital account, if the taxpayer adopts the method provided in section 174(a). See paragraph (b) of this section. If adopted, the method shall apply to all research and experimental expenditures paid or incurred in the taxable year of adoption and all subsequent taxable years, unless a different method is authorized by the Commissioner under section 174(a)(3) with respect to part or all of the expenditures. See paragraph (b)(3) of this section. Thus, if a change to the deferred expense method under section 174(b) is authorized by the Commissioner with respect to research or experimental expenditures attributable to a particular project or projects, the taxpayer, for the taxable year of the change and for subsequent taxable years, must apply the deferred expense method to all such expenditures paid or incurred during any of those taxable years in connection with the particular project or projects, even though all other research and experimental expenditures are required to be deducted as current expenses under this section. In no event will the taxpayer be permitted to adopt the method described in this section as to part of the expenditures relative to a particular project and adopt for the same taxable year a different method of treating the balance of the expenditures relating to the same project.

(b) *Adoption and change of method—(1) Adoption without consent.* The method described in this section may be adopted for any taxable year beginning after December 31, 1953, and ending after August 16, 1954. The consent of the Commissioner is not required if the taxpayer adopts the method for the first such taxable year in which he pays or incurs research or experimental expenditures. The taxpayer may do so by

claiming in his income tax return for such year a deduction for his research or experimental expenditures. If the taxpayer fails to adopt the method for the first taxable year in which he incurs such expenditures, he cannot do so in subsequent taxable years unless he obtains the consent of the Commissioner under section 174(a)(2)(B) and subparagraph (2) of this paragraph. See, however, subparagraph (4) of this paragraph, relating to extensions of time.

(2) *Adoption with consent.* A taxpayer may, with the consent of the Commissioner, adopt at any time the method provided in section 174(a). The method adopted in this manner shall be applicable only to expenditures paid or incurred during the taxable year for which the request is made and in subsequent taxable years. A request to adopt this method shall be in writing and shall be addressed to the Commissioner of Internal Revenue, Attention: T:R, Washington, DC, 20224. The request shall set forth the name and address of the taxpayer, the first taxable year for which the adoption of the method is requested, and a description of the project or projects with respect to which research or experimental expenditures are to be, or have already been, paid or incurred. The request shall be signed by the taxpayer (or his duly authorized representative) and shall be filed not later than the last day of the first taxable year for which the adoption of the method is requested. See, however, subparagraph (4) of this paragraph, relating to extensions of time.

(3) *Change of method.* An application for permission to change to a different method of treating research or experimental expenditures shall be in writing and shall be addressed to the Commissioner of Internal Revenue, Attention: T:R, Washington, DC, 20224. The application shall include the name and address of the taxpayer, shall be signed by the taxpayer (or his duly authorized representative), and shall be filed not later than the last day of the first taxable year for which the change in method is to apply. See, however, subparagraph (4) of this paragraph, relating to extensions of time. The application shall:

(i) State the first year to which the requested change is to be applicable;

(ii) State whether the change is to apply to all research or experimental expenditures paid or incurred by the taxpayer, or only to expenditures attributable to a particular project or projects;

(iii) Include such information as will identify the project or projects to which the change is applicable;

(iv) Indicate the number of months (not less than 60) selected for amortization of the expenditures, if any, which are to be treated as deferred expenses under section 174(b);

(v) State that, upon approval of the application, the taxpayer will make an accounting segregation on his books and records of the research or experimental expenditures to which the change in method is to apply; and

(vi) State the reasons for the change.

If permission is granted to make the change, the taxpayer shall attach a copy of the letter granting permission to his income tax return for the first taxable year in which the different method is effective.

(4) *Special rules.* If the last day prescribed by law for filing a return for any taxable year (including extensions thereof) to which section 174(a) is applicable falls before January 2, 1958, consent is hereby given for the taxpayer to adopt the expense method or to change from the expense method to a different method. In the case of a change from the expense method to a different method, the taxpayer, on or before January 2, 1958, must submit to the district director for the internal revenue district in which the return was filed the information required by subparagraph (3) of this paragraph. For any taxable year for which the expense method or a different method is adopted pursuant to this subparagraph, an amended return reflecting such method shall be filed on or before January 2, 1958, if such return is necessary.

§ 1.174-4 Treatment as deferred expenses.

(a) *In general.* (1) If a taxpayer has not adopted the method provided in section 174(a) of treating research or experimental expenditures paid or incurred by him in connection with his

trade or business as currently deductible expenses, he may, for any taxable year beginning after December 31, 1953, elect to treat such expenditures as deferred expenses under section 174(b), subject to the limitations of subparagraph (2) of this paragraph. If a taxpayer has adopted the method of treating such expenditures as expenses under section 174(a), he may not elect to defer and amortize any such expenditures unless permission to do so is granted under section 174(a)(3). See paragraph (b) of this section.

(2) The election to treat research or experimental expenditures as deferred expenses under section 174(b) applies only to those expenditures which are chargeable to capital account but which are not chargeable to property of a character subject to an allowance for depreciation or depletion under section 167 or 611, respectively. Thus, the election under section 174(b) applies only if the property resulting from the research or experimental expenditures has no determinable useful life. If the property resulting from the expenditures has a determinable useful life, section 174(b) is not applicable, and the capitalized expenditures must be amortized or depreciated over the determinable useful life. Amounts treated as deferred expenses are properly chargeable to capital account for purposes of section 1016(a)(1), relating to adjustments to basis of property. See section 1016(a)(14). See section 174(c) and paragraph (b)(1) of § 1.174-2 for treatment of expenditures for the acquisition or improvement of land or of depreciable or depletable property to be used in connection with the research or experimentation.

(3) Expenditures which are treated as deferred expenses under section 174(b) are allowable as a deduction ratably over a period of not less than 60 consecutive months beginning with the month in which the taxpayer first realizes benefits from the expenditures. The length of the period shall be selected by the taxpayer at the time he makes the election to defer the expenditures. If a taxpayer has two or more separate projects, he may select a different amortization period for each project. In the absence of a showing to the contrary, the taxpayer will be